

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
22 N Front St, Room 426
Memphis, TN 38103

Release Number: **201321032**

Release Date: 5/24/2013

MAR052007 ULL: 501.04-00

Legend:

ORG = Name of Organization

Date = xx

ORG

Person to Contact:

Identification Number:

Contact Telephone Number:

In Reply Refer to: TE/GE Review Staff

EIN:

Dear :

This is a Final Adverse Determination as to your exempt status under section 501(c)(4) of the Internal Revenue Code.

Our adverse determination was made for the following reasons:

ORG failed to establish that they meet the requirement for exemption under IRC 501(c)(4). Section 1.501(c)(4)-1(a)(1) and (2) of the Treasury Regulations reads in part, "(a) Civic organizations (1) *In general*. —A civic league or organization may be exempt as an organization described in section 501(c)(4) if: (i) It is not organized or operated for profit; and (ii) It is operated exclusively for the promotion of social welfare. (2) Promotion of social welfare (i) *In general*. —An organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements.

As a result of our recent audit of your organization's activities for the period ended December 31, 20xx, it was determined that a substantial part of your activities include the administration and enforcement of covenants for preserving the appearance of a particular area, the maintenance of common property, and the operation of pool and clubhouse facilities. Therefore, we are revoking your organization's exemption from Federal income tax under section 501(c)(4) of the Internal Revenue Code effective January 1, 20xx.

You are required to file Form 1120-H, U.S. Income Tax Return for Homeowners Associations. These returns should be filed with the appropriate Service Center for all years beginning after December 31, 20xx. Form 1120-H must be filed by the 15th day of the third month after the end of your annual accounting period. A penalty of \$20 a day is charged when a return is filed late, unless there is reasonable cause for the delay. However, the maximum penalty charged cannot exceed \$10,000 or 5 percent of your gross receipts for the year, whichever is less. This penalty

may also be charged if a return is not complete, so please be sure your return is complete before you file it. You are required to file Form 1120-H with the appropriate Internal Revenue Campus.

You have the right to contact the office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers. You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by calling or writing to: Internal Revenue Service.

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in the United States Tax Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels, gets prompt and proper handling.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely yours,

Marsha A Ramirez
Director, EO Examinations



DEPARTMENT OF THE TREASURY

Internal Revenue Service

TE/GE EO Examinations

1122 Town and Country Commons, Room 128
Chesterfield, MO 63017-8293

November 6, 2006

Legend:

ORG = Name of Organization

Address = Address of ORG

Date = xx

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

20xx12

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

ORG

ADDRESS

CERTIFIED MAIL — RETURN RECEIPT REQUESTED

Dear :

We have enclosed a copy of our report of examination explaining why we believe an adjustment of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018, *Consent to Proposed Adverse Action*. We will then send you a final letter modifying or revoking exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become final. In that event, you will be required to file Federal income tax returns for the tax period(s) shown above. File these returns with the Ogden Service Center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Local Taxpayer Advocate

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Internal Revenue Agent

Enclosures:

Publication 892

Publication 3498

Form 6018

Report of Examination

Envelope

Explanation of ItemsSchedule No. or
Exhibit

Name of Taxpayer

Year/Period Ended

ORG

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Legend:

ORG = Name of Org

Date = xx

1. Should the ORG, an organization exempt under Internal Revenue Code section 501(c)(4), continue to be exempt since it operates a swimming pool open only to the members of the organization?

FACTS

1. ORG was recognized, on 03/27/19xx, as an organization exempt under IRC 501(c)(4) because it was an organization described in IRC 501(c)(3).
2. The organization membership is compelled to belong by fees mandated in a covenant to the member's property title.
3. The organization owns and maintains common areas and a swimming pool.
4. The common areas and swimming pool are restricted to the organization's members and are not for the use and enjoyment of the general public.
5. The organization does not maintain a police (security) force or enact laws or other ordinances normally identified with a governmental subdivision or district.
6. The specific area which encompasses the organization's homeowner's property and common areas does not have its own zip code.

LAW

501(c)(4) of the Internal Revenue Code states that civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, will be recognized as exempt under subsection 501(a) if no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

Section 1.501(c)(4)-2 of the Income Tax Regulations states that an organization will be regarded as operating exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community, because it is operated primarily to bring about civic betterments and social improvements.

Section 1.501(c)(4)-1(a)(2)(ii) of the regulations provides that an organization is not operated primarily for the promotion of social welfare if its primary activity is operating a social club for the benefit, pleasure, or recreation of its members.

Rev. Rul. 73-306, 1973-2 C.B. 179 provided that a nonprofit organization formed to protect the rights of tenants in one rental complex did not benefit the community in general, but rather a select group of individuals. Therefore, exemption under 501(c)(4) was denied.

REV-RUL, Homeowners association, preserving appearance and maintaining common areas, Revenue Ruling 74-99, 1974-1 CB 131, (Jan. 01, 1974)

A homeowners association, to qualify for exemption under section 501(c)(4) of the Code, (1) must serve a "community" which bears a reasonable recognizable relationship to an area ordinarily identified as governmental, (2) it must not conduct activities directed to the exterior maintenance of private residences, and (3) the common areas or facilities it owns and maintains must be for the use and enjoyment of the general public; Rev. Rul. 72-102 modified.

Explanation of Items

ORG

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Rev. Rul. 74-99, 1974-1 C.B. 132 clarified the definition of community as it applies to homeowners associations. A mere aggregation of homeowners in a real estate subdivision is not a community. It must be a geographical unit bearing a reasonably recognizable relationship to an area ordinarily identified as a governmental subdivision or a unit thereof.

REV-RUL, Homeowners' associations, Revenue Ruling 80-63, 1980-1 CB 116, (Jan. 01, 1980) was issued to discuss, in question and answer format, certain issues raised by Rev. Rul. 74-99.

Question 1:

Does Rev. Rul. 74-99 contemplate that the term "community" for purposes of section 501(c)(4) of the Code embraces a minimum area or a certain number of homeowners?

Answer: No. Rev. Rul. 74-99 states that it was not possible to formulate a precise definition of the term "community". The ruling merely indicates what the term is generally understood to mean.

Question 2:

May a homeowners' association, which represents an area that is not a community, qualify for exemption under section 501(c)(4) of the Code if it restricts the use of its recreational facilities, such as swimming pools, tennis courts, and picnic areas, to members of the association?

Answer..

No. Rev. Rul. 74-99 points out that the use and enjoyment of the common areas owned and maintained by a homeowners' association must be extended to members of the general public, as distinguished from controlled use or access restricted to the members of the association. For purposes of Rev. Rul. 74-99, recreational facilities are included in the definition of "common areas".

Rev. Rul. 80-206, 1980-2 C.B. 185 provided that a nonprofit organization formed to protect the legal rights of all the tenants in a community does qualify as a social welfare organization.

Flat Top Lake Association v. United States, 868 F.2d 108 (4th Cir. 1989), the court concluded that a homeowners' association that encompassed a very large area but restricted use of its facilities to its members does not qualify for exemption under IRC 501(c)(4). The court went on to conclude that in order to be exempt under IRC 501(c)(4), the organization must be a community that constitutes an active part of society rather than a private refuge for those who would live apart.

GOVERNMENT'S POSITION

Civic leagues and organizations not organized for profit, but operated exclusively for the promotion of social welfare are recognized as exempt under section 501(c)(4) of the Code. An organization will be regarded as operating exclusively for the promotion of social welfare if it is primarily engaged in promoting the common good and general welfare of the people in the community (Section 1.501(c)(4)-1(a)(2)(i) of the regulations).

One crucial element for section 501(c)(4) exemption is promotion of social welfare for the people of a community. The Service granted exempt status to an organization that defended tenants' rights for a whole community, which is

Name of Taxpayer

Explanation of Items

Schedule No. or

E x h i b i t

Year/Period Ended

ORG

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considered an exempt activity. Rev. Rul. 80-206. In comparison, the organization in Rev. Rul. 73-306, was denied exempt status because it only benefited the tenants in one rental complex. It did not benefit the community in general, but rather a select group of individuals.

Rev. Rul 74-99 noted that an aggregation of homeowners in a real estate subdivision is not a community. It must also be a geographical unit bearing a reasonably recognizable relationship to an area ordinarily identified as a governmental subdivision or district. This organization is not a community as described above since it is not a recognized governmental subdivision or district and does not possess the powers or responsibilities (i.e., police protection) generally associated with such entities.

Rev. Rul. 80-63 further provides that an area not considered a community cannot be exempt under 501(c)(4) if it operates a swimming pool for the exclusive use of its homeowner members. *Flat Top Lake Association v. United States* reinforces this ruling by concluding that for an area to be considered a community it must be an active part of society rather than a private refuge for its members.

Considering all the facts and circumstances and applying the applicable law the ORG is not an organization described in IRC 501(c)(4) of the Code. However, it may qualify as a homeowners association under section 528 of the Code.

TAXPAYER'S POSITION

The organization agrees with the Government's position.

CONCLUSION

The organization's exemption under section 501(c)(4) of the Code should be revoked for the period beginning January 1, 20xx and for all subsequent periods. If the organization elects, and is eligible under section 528 of the Code, it may begin filing Form 1120-H. Otherwise it must file Form 1120.